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The Open Method as a New Mode of Governance: The Case of Soft Economic Policy Co-ordination

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Abstract

Taking economic co-ordination in EMU as a starting point, this article explores the development of the open method of co-ordination, addressing whether it is a new form of governance from two related perspectives. First, to what extent can the method be effectively applied outside the scope of economic policy? Second, will it lead to policy transfer to the EU and hence act only as a transitional mode of governance? Identified at the Lisbon European Council, the method codified practices such as benchmarking, target-setting and peer review developed in the Luxembourg, Cardiff and Cologne processes. The method offers a new approach to governance of the EU as a heterarchical, decentred and dynamic process. It supports and radicalizes the principle of subsidiarity; offers an alternative to the treaty rules on enhanced cooperation; and addresses some of the legitimacy issues inherent in the EU. In EMU, the method arose out of a specific policy framework with a common monetary policy complemented by the co-ordination of national economic policies. The recent recommendation issued against Ireland is the first example of the operation of the method in EMU and shows how debate can be stimulated and how different and arguably equally valid perspectives defended. The particular experience of EMU with a sound money, sound finance paradigm, a long history of project-building by key elites and the central role of the European Council suggest similar conditions are required for the effective application of the method in other policy spheres. The context within which the method has operated to date is contingent and could change either over time or between policy fields. If so, the very openness of the method may serve to reconfigure the boundaries of competence between the Member States and the Union, after all.

Introduction

The open method of co-ordination referred to in the Lisbon summit conclusions is not unprecedented. Co-ordination has been present in the Treaty since 1958 where Member States promised to co-ordinate their economic policies² while co-ordination of employment issues emerged in the 1970s when the largely ineffective Standing Employment Committee was set up (Goetschy, 1999). Both the European employment strategy adopted at Essen in 1994 (Council, 1994) and the

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² Art. 103 EEC.

macroeconomic monitoring procedures introduced in Maastricht³ further developed state co-operation, with Essen eventually formalized by the inclusion of an employment chapter at Amsterdam. Co-ordination in these two policy spheres became more explicit, far-reaching and complex following the establishment of the euro-zone. The processes established following the Luxembourg, Cologne and Cardiff European Councils frame the context within which co-ordination takes place and have become codified as the 'open method'. Other forms of co-ordination arose in other spheres. In justice and home affairs (JHA), practices outside the European Community (EC) such as the Trevi Group and Schengen, acted as laboratories for the development of European Union (EU) policy eventually encapsulated in the third pillar (Monar, 2001; Wallace, 2001). In the defence sphere, driving factors such as the collapse of the Berlin Wall and the Yugoslav wars highlighted the need to redefine European defence institutions and policy, prompting further co-operation culminating in the embryonic but politically significant common European security and defence policy (CESDP) (Howorth, 2001; Wallace, 2001). While there is some evidence of open coordination in justice and home affairs (Commission, 2001d), the need for tightly knit joint planning and shared doctrines calls for a more focused and less open form of co-ordination in relation to defence policy (Wallace, 2001).

This article takes economic co-ordination in the context of economic and monetary union (EMU) as its starting point for an exploration of the development of the open method of co-ordination. It addresses the question of whether this method is a new form of governance from two related perspectives. First, to what extent can the open method be applied outside the scope of economic policy; and, second, will it ultimately lead to transfer of competence to the EU and hence act only as a transitional mode of governance? Wallace sets out a useful framework for discussing the novelty of the open method:

In the early years the Commission used this technique [co-ordination] to develop light co-operation and co-ordination in order to make the case for direct policy powers ... Latterly we can see that this approach of co-ordination, strengthened by the contemporary fashion for 'benchmarking', is being developed not as a transitional mechanism but as a policy mode in its own right The object is not to establish a single common framework, but rather to share experience and to encourage the spread of best practice. There are some grounds for expecting this to be a typical mode in future EU policy-making as an alternative to the formal re-assignment of policy powers from national to EU level'. (Wallace, 2000, p. 33).

The novelty of the open method in EMU is closely associated with an economic paradigm that puts paid to any notion of direct transfer for matters of factor market flexibility. This does not mean that the method is sui generis, since the central thrust of the Lisbon Conclusions was to extend it to other policy sectors. The method developed in economic policy because of the existence of certain conditions such as: dominant theoretical framework(s); agreed principles or goals for one policy that make co-ordination in others important; a history of project-building by key elites who also co-ordinate the new policy area; and a commitment by the Council through the explicit articulation of support for the approach. The extent to which the method can be successfully applied to other policies depends on the extent to which these or similar factors exist.

³ Art. 99 EC.

There are three reasons why the open method may be seen as a new mode of governance. First, taking developments in economic policy as our case study, the open method emerged to deal with the specific issue of factor (capital and labour) and product market flexibility under EMU. Within the current paradigm of sound money and sound finance, national responses in the framework of commonly agreed parameters to this issue are deemed superior to either uncoordinated national action or action via the traditional and more legally structured Community method. Second, as EU policy-making moves into politically sensitive areas such as immigration, defence and taxation, the centralization of policy formation encapsulated in the Monnet method is more problematic due to difficulties in achieving policy convergence and popular dissatisfaction with the Union. This has prompted the development of new methods of governance that facilitate further Europeanization outside existing institutional forms. Third, the open method provides a pragmatic rather than a principled answer to the Achilles' heel of the EU – legitimacy. Legitimation is presumed for policy formed at the national level and, even if contested, arguments are framed in national rather than EU terms and hence are unlikely to call into question fundamentally the role of the EU in facilitating co-ordination. It is, however, debatable whether the open method transcends the usual criticisms of governance in the EU, notably elitism and opacity.

Whether the open method is merely a transitional mechanism of governance is answered in part by Dyson's view that it is intended to bring about a convergence in policy-makers' attitudes towards specific issues. ' "Bench- marking" can be a factor in reframing domestic discourse and shifting the distribution of power over ideas and agenda setting' (Dyson, 2000a, p. 5). This suggests that the sound money, sound finance paradigm is currently seen as a necessary truth, although such truths can become contingent in the presence of a changing conceptual paradigm. For example, the view that the heterogeneous nature of national economies made monetary union impossible was prevalent in many states in the years before EMU. Once member governments accepted the sound money, sound finance paradigm for monetary policy, other pre- existing barriers, such as diversity in national economies, were surmounted. Arguably, as common values begin to grow (through the open method), the possibility of a transfer in competence to the EU level could increase. If this happens, the open method would be transitional and its novelty as a mode of governance would diminish.

The article first describes the open method of co-ordination and why it has arisen in the context of EMU, before locating it in the broader context of EU governance. The institutional and organizational complexity and the importance of key conditions for the operation of this form of co-ordination are explored, including recent events concerning Ireland, to show the operation of soft policy approaches and the limitations of peer pressure and soft law measures. The article then returns to the core argument: that the open method is a new mode of governance subject to two caveats. First, as the experience of EMU illustrates, the open method is most applicable to a policy sector when certain conditions are met. Second, even where the possibility of transfer of competence to the EU seems unlikely in a given policy sector, it cannot be discounted entirely. The possibility of such transfer is conditional on the given context in which the policy is formulated. By modifying this context over time, the open method could perhaps serve to reconfigure the boundaries of competence between the Member States and the Union.

I. The Open Method of Co-ordination

The term 'open method of coordination' stems from the Lisbon European Council, but draws its inspiration from earlier Council meetings at Luxembourg, Cardiff and Cologne, where a series of supply-sided policy initiatives were set up. The emphasis is on consensus-forming with three elements found in each process: common assessment of the economic situation; agreement on the appropriate economic policy responses; and acceptance of peer pressure and, where necessary, adjustment of the policies being pursued (Commission, 2001, para. 2). The Luxembourg process implements the provisions in the employment chapter of the Treaty. It is designed to boost the efficiency of labour markets by improving employability, entrepreneurship, adaptability (on both sides of industry) and equal opportunities for men and women when searching for gainful employment. The process is implemented through an annual cycle, which begins with the European Council adopting the 'employment guidelines' for the whole Union that set employment policy priorities. These guidelines avoid the delineation of any common course of action, preferring instead to enable national policy initiatives. Thus each state is responsible for formulating its national action plan, which specifies how it will pursue the guidelines. The Commission and Council then assess the national action plans in a joint employment report, passing legally non-binding recommendations, where necessary, on the performance of individual states (Goetschy, 2000). Thus, the Luxembourg process draws on a spirit of mutual learning, benchmarking, best practice and peer pressure to achieve its objectives.

The Cardiff process is similar, although structural policy has a broader remit addressing product, service and capital markets, labour markets and long-term public finances, and hence is a more daunting and long-term project than the more focused issue of employment policy. Like the Luxembourg process, the Cardiff process reflects the view that, although member governments face similar challenges with respect to structural reform, the optimal course of action lies at the national level. The process began with the publication of national reports by each government on its product and capital markets. The Commission supplemented these with two reports on progress in and challenges for, capital, product and labour markets, and public finances respectively. This assessment, which is now repeated annually on a modified basis is designed to feed into the preparation of the Union's broad economic policy guidelines, the aim being co-ordination of national responses through a system of benchmarking, best practice, recommendations and periodic monitoring.

Finally, the Cologne process brought the Luxembourg and Cardiff processes together with the macroeconomic dialogue under the heading of the European Employment Pact. The macroeconomic dialogue consists of bi-annual discussions of the policy-mix at the EU level between the social partners, the European Central Bank, the Commission and Council. The dialogue has no legislative powers, nor does it issue recommendations or even publish minutes. It is designed as a confidence-building measure for participants through confidential exchanges of ideas with a view to improving the Union's overall economic policy mix.

The open method of co-ordination was explicitly identified as a form of governance at the Lisbon European Council, thus codifying practices developed in the Employment Pact (European Council, 2000). The innovation at Lisbon was that these practices were to be applied in other policy spheres and in the light of the ten-year goal of the EU becoming the most competitive and dynamic knowledge-based

economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion. The naming and adoption of the method is recognition that what was happening in the economic sphere is new in the wider context of EU governance. The Council described the open method as a vehicle for spreading best practice and achieving greater convergence towards the main EU goals (European Council, 2000a; Commission, 2001c, p. 21). It has four key elements:

- setting short-, medium- and long-term guidelines for the EU with specific timetables for their achievements;
- establishing performance indicators and benchmarks tailored to each Member State and different sectors which allow comparison of best practice;
- translating targets from the European to the national and regional levels; and
- periodic monitoring, peer review and evaluation with the emphasis placed on the process of mutual learning.

‘Open’ can refer to state action, policy outcome or à la carte involvement by states. Targets are set for the Union, but national responses are formulated at the national level with no threat of formal sanction. The commitment to this decentralized approach is made explicit in the Lisbon Conclusions (European Council, 2000a, para. 38). With regard to outcomes, the comparatively vague nature of the policy targets in the open method introduces uncertainty about likely consequences and whether or not state-centric governance will remain the norm. So far, the method concerns all Member States, whether in the eurozone or not. The method is designed not only to deliver policy outcomes, but also to act as a process for improving policy formation. Benchmarking, which goes to the heart of the open method, became widespread in industry and was pushed as a tool for guiding EC policies by the European Round Table of Industrialists (Sisson and Marginson, 2001, p. 2; Wallace, 2001). National policy-makers began to use benchmarking in the 1980s. At the same time persistent high levels of unemployment throughout the EU prompted calls for co-ordinated action, while the start of the third stage of EMU created further impetus for closer co-ordination of economic policy. The Irish Presidency saw the attraction of benchmarking that allowed working towards common goals without encroaching on national sovereignty, thus promoting a technique common in the OECD (and thus familiar to the Member States) (Wallace, 2001). Benchmarking has no accepted definition (Public Sector Benchmarking Service, 2001) although the emphasis in the open method on understanding how it is that others operate and why it is they behave in a particular manner in the light of agreed guidelines – through such practices as reverse engineering – falls within a broad understanding of the term.

As can be seen from Table 1, the open method is linked to a variety of policies where states are capable of proceeding individually, but are unsure of the best path to take, where collective action is needed for any reform, or there are increased returns from such collective action (Mosher, 2000). The method institutionalizes the sharing of experience and reform experimentation, removing any real or apparent risk of regulatory competition and replacing it with a co-operative but non-binding method. In some sectors, such as information society, policy initiatives have been launched, while in others, such as research, initiatives remain at the preparatory stage. The

method is being applied in new areas, such as pension reform and education policy (Council, 2001, paras 32 and 10) and elements of the method (benchmarking, peer review) can be seen in the Lamfalussy Report and its proposals for regulation of an integrated European securities market (Lamfalussy, 2001).

Table 1: The Open Method of Co-ordination in Action

Origin	Policy	Description
Lisbon European Council, 2000	Lisbon European Council, 2000	Benchmark implementation of the March eEurope action plan. Ensure actions are carried out efficiently, effectively and with a high profile. Implementation of the plan in each Member State reviewed annually at the spring European Council
Lisbon European Council	Research policy	Benchmark national research and development policies. Identify indicators for assessing performance in different fields with a view to developing a European research area. Commission to draw up a European innovation scoreboard and a map of research excellence
Lisbon European Council	Entrepreneurial policy	Benchmark the process of starting a business in each Member State. The Commission to devise a coordinated strategy to simplify the Union's regulatory environment
Lisbon European Council	Social policy	Member States to draw up national action plans on poverty and social exclusion by June 2001; to devise indicators for assessing progress and policy mechanisms for enforcing the Union's objectives in this area
Feira European Council, June 2000	Enterprise policy	To complete a review of how the interests of small businesses are represented at EU and national level, including through the social dialogue
Stockholm European Council, March 2001	Education policy	To present a detailed work programme on the follow-up of the objectives of education and

		training systems, including an assessment of their achievement at the national level
Stockholm European Council	Enlargement	To develop ways and means of actively involving the candidate countries in the goals and procedures of the Lisbon strategy
Stockholm European Council	Pension reform	To apply the open method to ensure the adequacy of health care, the care of the elderly and pension systems

The Union is committed to involving candidate countries in the Lisbon strategy. While such commitment is not yet supported by action, the open method has been applied to accession countries in practice in the joint action plans. Under these plans the candidate country draws up a national action plan to prepare its jobs market for EU membership, which is then jointly reviewed by its own government and the European Commission. Legally non-binding recommendations can be issued against the country when necessary. For example, when assessing Estonia's national action plan recently, the Commission praised restructuring efforts, but drew attention to remaining structural rigidities in Estonia's labour market and the need for education and training (Commission, 2001a). The influence of the open method can be seen in the Baltic region. In 1999 Denmark, Estonia, Latvia, Lithuania, Poland and Russia launched the Baltic Sea region sector programme on labour-market policy, modelled on the European Employment Pact and motivated by significant labour market challenges in the region, notably high levels of unemployment. The objective of the programme is to achieve 'policy integration' for the labour market by sharing experiences and exchanging best practice (Arbejdsministeriet, 1999).

The open method is similar to policy transfer, i.e. a process in which 'governments study each other's different methods, gauge the success of various policy alternatives and mimic best practices employed elsewhere, with successful policies transferred deliberately and willingly' (Bomberg and Peterson, 2000, p. 6). Dolowitz and Marsh distinguish between three broad varieties of policy transfer. First, voluntary transfer is primarily motivated by dissatisfaction on the part of policy-makers with existing policy arrangements. Second, direct coercive transfer occurs when one government compels another to adopt a certain policy. Finally, indirect coercive transfer arises when the presence of externalities or functional interdependencies leads to joint action on the part of policy-makers. Within the context of EMU, the open method most closely resembles the indirect coercive strain of policy transfer, since national labour market developments are now treated as matters of mutual concern owing to their potential effects on euro-zone monetary policy. While functional interdependence is present, the question remains to what extent successful policies will in fact be transferred between states. For example, the heterogeneity of euro-zone labour markets is such that one Member State's meat could, if applied in a significantly different context, quickly amount to another Member State's poison. Within EMU,

the open method conforms less to the notion of policy transfer and more to the definition of lesson drawing, according to which ‘lessons are drawn from other places or times which do not necessarily result in policy or institutional change’ (Dolowitz and Marsh, 1996, p. 344). In considering the novelty of the open method beyond the policy domain of EMU, therefore, the differences between transitional and terminal modes of integration, on the one hand, and policy transfer and lesson drawing on the other, appear to be largely commensurate.

II. Governance and the Open Method of Co-ordination

The open method can be seen as a new approach to governance in the light of three characteristics of governance in the EU: the principle of subsidiarity, flexibility and legitimacy. The Single European Act strained the original EU governance model with its emphasis on centralization, functional segmentation and vertically integrated structures (Lebessis and Paterson, 2001, p. 268). The deregulatory ethos in the rulings of the European Court, with an emphasis on removal of what in retrospect appear obvious barriers to trade, was largely unproblematic. With the Single Act, an ambitious legislative agenda identified the Community as a rule-setter on a grand scale (Calingaert, 1999). This agenda of positive integration, combined with greater use of qualified majority voting, raised questions as to the authority of the EC encapsulated by reference to the democratic deficit. The centralized system of governance did not adequately address the interests of the ‘peoples of Europe’, already at one remove from the EC. Increasingly complex policy formation, as a result in part of functional segmentation within the Council and the myriad of committees responsible for the tide of secondary legislation, served further to render the system opaque, distant and apparently unaccountable (Vos, 1997). New systems of governance needed to be found to address these concerns (Commission, 2001c).

One response was the introduction of the principle of subsidiarity in the Treaty of Maastricht. The principle⁴ determines the level of government at which decisions are taken in the EU (van Kersbergen and Verbeek, 1994). Concerned only with the Member States/EU axis, but developed to cover the strength of the legal norm that is used and as the basis for simplification of existing legislation, it is not clear to what extent the principle has impacted on policy formation (Maher, 1996). Nonetheless, it now forms an important part of the cultural frame within which policy formation takes place and is a tool in deciding whether or not particular action should be taken by the EU (de Búrca, 1999). The open method seems entirely consistent with the principle, with its emphasis on policy learning among different levels of government. The Lisbon Conclusions themselves note that a fully decentralized approach will be applied in line with the principle (European Council, 2000a, para 38). Arguably, the open method goes further and radicalizes subsidiarity; this is a static principle with its focus on what level of government at a particular time of rule formation in the policy process and with a continuing emphasis on hierarchy of structures. The open method, being focused on horizontal learning processes and peer pressure where individual action runs counter to broadly accepted principles, is dynamic in nature, heterarchical, decentred as a *modus operandi* and without any particular rule or single policy objective as an objective (Lebessis and Paterson, 2001, p. 292).

While co-ordination in the economic sphere addresses anxieties surrounding centralization in the light of positive integration, it replicates problems of functional

⁴ Art. 5 EC and Art. 1 TEU.

segmentation with a multiplicity of systems and a web of institutional interrelationships combining hard and soft co-ordination and with an intergovernmental edge (Wessels and Linsenmann, 2001), problems also found in justice and home affairs (Monar, 2001). Co-ordination is built into the Treaty for economic, fiscal and employment policies with a system of guide- lines and multilateral surveillance that can culminate in an adverse Council recommendation (or ultimately a fine under the excessive deficit procedure in relation to fiscal policy).⁵ The Council assumes a key role in relation to coordinating processes both in terms of their functioning and, at the level of the European Council, in wider questions of system design, timetabling and policy objectives. The Euro-group, an informal grouping of euro-zone finance ministers with no law-making powers, also has the capacity to ensure co- ordination (Jacquet and Pisani-Ferry, 2001). The Commission's role of anal- ysis, neutrality and synopsis (Commission, 2001b, para. 13) is different from under the classic Monnet method and arguably weakened with its usual agenda-setting function reduced (Hodson and Maher, 2000b). It can trigger a number of procedures, but the trigger is a recommendation and not a proposal, and hence can be modified by qualified majority voting in Council rather than unanimity (Harden, 1999, p. 81). Its weakness may follow from the debacle of the Santer Commission's resignation, but more specifically, from the emphasis on implicit and bottom-up policy co-ordination (Dyson, 2002a), signalled by the lukewarm reception to its communication on co-ordination (Commission, 2001b). This position could change given the capacity of the Commission historically to augment its role. It can contribute to effective co-ordination and gain influence through fulfilling a secretariat role and providing key intellectual resources, particularly given the rather clumsy nature of the processes (Jacquet and Pisani-Ferry, 2001, p. 14; Goetschy, 1999). In its White Paper on Governance, the Commission notes its existing active role in the open method and its desire to remain active in the future, but warns against the method upsetting the institutional balance notably by marginalizing the European Parliament. Thus it suggests there should be a regular reporting mechanism for the Parliament so as to maintain the existing institutional balance (Commission, 2001c, p. 22).

There are three main Council committees involved in the open method. The Economic and Finance Committee, an advisory committee, is the most important. It prepares the Council of Economic and Finance Ministers (Ecofin) meetings, and has consultative and review functions, being responsible for the preparation of the broad economic policy guidelines and for the co-ordination of fiscal policy through the operation of the Stability and Growth Pact (Hodson and Maher, 2000b). The more recently established Employment Committee monitors employment policy under the Luxembourg process.⁶ The Economic Policy Committee monitors structural policy under the Cardiff process; is responsible for the macroeconomic dialogue; and helps formulate the broad economic policy guidelines, as well as contributing to the multilateral surveillance that flows from them.⁷ Policy areas overlap, e.g. one of the concerns of the Union is that of the ageing population, which raises issues touching on all three areas with co-ordination across committees dependent on chairs maintaining contact and exchanging information informally before reporting to

⁵ For the excessive deficit procedure see Art. 104 EC; Regulation 1466/97 OJ L 209, 2.8.97, p. 1; Regulation 1467/97 OJ L 209, 2. 8. 97, p. 6 and Resolution of the European Council on the Stability and Growth Pact, OJ C 236, 2.8.97, p. 1.

⁶ Art. 130 EC, Council Decision 2000/98/EC OJ L 29, 24.1.00, p. 21.

⁷ Annex to the Council Decision 2000/604/EC of 11.10.2000 on the composition and the statutes of the Economic and Policy Committee OJ L 257, p. 30.

Council. Additional committees also may be created. The Nice Treaty requires the establishment of a Social Protection Committee to promote co-operation between the Commission and Member States on social protection policies,⁸ thus making social protection the third side of a welfare policy triangle with the related but separate sides being macroeconomic policy and employment policy (Rhodes, 2000).

The difficulties of demarcation of responsibility and the interaction of the committees (save through their shared function of reporting to Ecofin), underlines the opacity and complexity of the institutional framework, with the Commission recommending greater visibility (Commission, 2001b, para. 4). It is perhaps incongruent to discuss opacity in a system dependent on transparency for its effectiveness, but the processes are simultaneously transparent and opaque in different ways. The opaque nature of the processes is partly due to their number and their complex institutional framework. It is also due to their relative novelty within the governance structures of the EU, with the emphasis on process, rather than outcome. The absence of hard law also renders the system opaque, with only soft law measures available outside the scope of the excessive deficit procedure, and with the attendant uncertainty as to their status or consequences. Transparency is essential for the processes, as learning is dependent on information exchange. However, the fragmentation of responsibility means the system lacks transparency beyond the core of elites – national and Community civil servants and the social partners through the macroeconomic dialogue – who are directly involved in preparing and discussing national reports, and in framing of broad guidelines. While this characteristic may be similar to that found within national policy-making processes, the issue is of greater concern in the EU where problems of legitimization are seen as more intractable.

The open method can also be seen as a form of ‘soft’ flexibility in contrast to that found under Art. 11 EC and Art. 40–43 EU. These provisions allow for closer co-operation between states aspiring to greater integration than is currently envisaged under the treaties, by setting down specific steps that have to be taken in order to protect the interests of non-participants and the *acquis* (de Areilza, 1998; Philippart and Edwards, 1999). The provisions have yet to be invoked, although amendments introduced in Nice may change that,⁹ while the Commission has suggested their adoption specifically in relation to economic policy co-ordination (Commission, 2001b, para. 18). Even with reform, the provisions form a legal straitjacket determining how much further co-operation can take place and reflect an anxiety about the ability of the EU to control outcomes. This can be contrasted with the open method that occurs in a space devoid of formal legal norms apart from the Treaty provisions themselves and the decisions establishing the relevant committees. There is no formal attempt to control outcomes (outside of fiscal policy of course), and process is determined by a system of benchmarking and lesson-drawing, emphasizing state competence and the voluntary alignment of policies. Thus, the open method provides real flexibility and marks a further maturation of the integration process. The desire of the EC to control outcomes, as manifest in the directive as the rule of choice in the single market, with its emphasis on common outcomes if not methods,¹⁰ is overcome by recognition of the importance of diversity at the national level in relation to policy formation, legal frameworks, ideational references and popular perceptions and

⁸ Art. 2(11) Treaty of Nice replacing Art. 144 EC.

⁹ Art. 1(9)–(13) and Art. 2(1) Treaty of Nice, replacing Arts. 40–43 TEU and Art. 11 EC respectively.

¹⁰ Art. 249 EC.

reactions to either the European project generally or the specific policy being co-ordinated.

Finally, the open method goes some way to solving the intractable problem of the legitimacy of policy-making in the EU (Hodson and Maher, 2000b). Legitimation is presumed for national policy where it enjoys democratic endorsement, popular sovereignty being the legitimate source of power for the exercise of authority (Obradovic, 1996, p. 195; Verdun and Christiansen, 2000, p. 171). Even if a particular policy decision at the national level reflects learning through the open method, the system is one of *ex ante* implicit co-ordination rather than explicit co-ordination (Dyson, 2000a, p. 42) and, in the absence of the imposition of explicit obligations or sanctions, it is difficult to question the legitimacy of the rather tangential role of the EU in economic policy formation. On the other hand, the Union may have only limited success in claiming credit for policy outcomes, and the attendant legitimation that flows from that, where its role is so tangential. In fact, legitimacy questions could be raised even within the current framework. If a state is subject to a critical recommendation from the Council, then its government could 'play the legitimacy card'. The absence of legal norms undermines any legitimacy of the process at the EU level – the rule of law being one, albeit flawed, means of securing legitimacy. The open-ended nature of the method allows for diversity and the government's democratic mandate legitimates its dissenting voice in the light of any adverse recommendation for breach of the broad economic policy guidelines. At the same time, dissenting voices within the state may take up the alternative stance proffered by the EU, thus prompting debate which has the capacity to shed light on the policies, processes and principles underlying them.

If co-ordination leads to a policy shift to the EU, then the national democratic credentials will be lost and the well-rehearsed arguments about the legitimacy of the EU – lack of a democratic legitimacy; no constitutional mandate framing shared identity and values; the conditional legitimacy of outputs – may re-emerge (Hodson and Maher, 2000b). Shared values usually equate with some sort of constitutionalization and the difficulty here is that the sound money and sound finance paradigm is one that is not constitutionalized to the same degree in all Member States; see, e.g., the recent Irish example and compare with the attitude to sound money in Germany. The extent to which there is a discrepancy in the embeddedness of that paradigm means that, if the economic climate becomes more difficult, the paradigm itself could be questioned and incompatible policy stances emerge which undermine policy co-ordination. Alternatively, it could be argued that the paradigm would really become embedded only when it is embraced as a vital anchor in times of economic difficulty.

Thus the emphasis on national policy responses, the explicit recognition of the competence of the Member States in this field, the absence of closure in terms of outcome all point to a process embedded in a national democratic framework. At the same time, how co-ordination develops, both in terms of the exertion of peer pressure against a recalcitrant state and in the adoption of unpopular national policies inspired by co-ordination, may allow the question of legitimacy to be raised in relation to the EC processes.

III. Why has the Open Method of Co-ordination Developed in Relation to Economic Policies?

EMU involves a direct transfer of monetary sovereignty from the national to the Union level (Alesina and Grilli, 1992; Bean, 1998; Buti and Sapir, 1998). Such sovereignty now rests with the Eurosystem of (participating) national central banks and the supranational European Central Bank (ECB). EMU is not however, solely a monetary phenomenon nor a single rule exercise (Wessels and Linsenmann, 2001). The loss of national monetary and exchange-rate policies significantly alters the nature of macroeconomic policy-making in the euro-zone (Allsopp and Vines, 1998). National authorities may no longer turn to such instruments when faced with an asymmetric economic disturbance (Eichengreen, 1998). The burden of adjustment is transferred on to such alternative instruments as budgetary stabilizers, or wages and prices (Begg and Hodson, 2000). At the same time the creation of a currency zone substantially deepens economic integration, thus increasing the scope for both institutional and regional spillover (Bayer, 1999). Institutional spillover arises from a situation in which a single monetary institution faces 12 separate national economies. Divergence between the policy preferences of the ECB and those of all or some national fiscal authorities could present a barrier to the achievement of price stability (Ardy, 2001). No matter how credible the ECB appears, stable prices are increasingly difficult to achieve where there are, for example, loose inflationary fiscal policies. Wage developments at the national level also have an effect on euro-zone inflation and thus national wage setting mechanisms are of some concern to the ECB (Kilponen et al., 1999).

EMU also strengthens the ties between national economies such that national policy effects are now felt more in the euro-zone, creating the risk of regional spillover (Gros and Thygesen, 1998). Previously, an increase in the deficit spending of, say, Italy may have yielded higher Italian interest rates. The same action now may trigger a rise in euro-zone interest rates. This means that the entire euro-zone would pay the price for Italy's fiscal profligacy. From an Italian perspective, the cost would be spread among its peers, thus diluting the strength of previous incentives for fiscal rectitude.

The Union has responded to fears of institutional and regional spillover through a combination of 'hard co-ordination' in fiscal policy and 'soft co-ordination' in economic policy (Wessels and Linsenmann, 2001). Both forms of co-ordination arise out of Member States' commitment to treat their economic policies as a matter of common concern and to co-ordinate them in the Council with a view to achieving *inter alia* sustainable and non-inflationary growth.¹¹ If economists have generally welcomed the principle of such co-ordination under EMU, they have failed to agree on the precise form that it should take (Mooslechner and Scheuez, 1999).

The Treaty eventually delivered a monetarist vision of EMU in which policy is dominated by a supranational and independent European Central Bank, driven by the primary objective of maintaining price stability. The economic dimension of EMU falls far short of the Werner Report (Commission, 1970), with an intergovernmental commitment by Member States to regard their economic policy as a matter of mutual concern (Dyson, 2000a). This represents a rejection of the parallel principle, according to which a transfer of national monetary policies to the European level is matched by an analogous assignment of economic policies (Dyson, 2000a, p. 32). From the perspective of political economy, this rejection has been attributed to a lack of appetite amongst the Member States for further political integration (Verdun and Christiansen, 2000). While the lack of such support is well documented, the political

¹¹ Art. 2 EC.

economy perspective can overstate the extent to which current arrangements under EMU are second best and arguments have been made in defence of EMU's existing macroeconomic credentials. Such arguments suggest that, given the radical differences between euro-zone economies with respect to production, structure and labour market flexibility, a single adjustment response seems unworkable and adjustment mechanisms at the national level seem preferable, since they are better suited to their economy's own specificity (Mayes and Viren, 2000). Supranational measures are required only to avert negative spillover. A belief in this logic pervades a policy architecture characterized by supranational institutions, institutional linkages, common policy and both hard and soft policy co-ordination.

The risk of regional spillover is addressed primarily through hard co-ordination in the Stability and Growth Pact, where co-ordination is associated with convergence towards predetermined targets (Jacquet and Pisani-Ferry, 2001, p. 10). States agree to maintain their budget deficits within 3 per cent of GDP and their medium-term budgetary position close to balance or in surplus (Wessels and Linsenmann, 2001). The Pact is enforced through multi-lateral surveillance and the excessive deficit procedure. The former requires each Member State to formulate a stability programme (or convergence programmes in the case of states outside the euro-zone), for national economic policy that conforms to the spirit of the pact. Compliance with the terms of the pact leaves room for budgetary manoeuvre in the face of an asymmetric economic disturbance (Artis and Buti, 2000). In the event of deviation from the spirit of the pact, the Council can issue a recommendation for corrective action. In the event of an infringement of the pact, the excessive deficit procedure can be triggered, culminating in formal sanctions, including fines.

The risk of institutional spillover is addressed by opening channels of communication between existing supranational bodies. A representative of the ECB attends meetings of the Ecofin, while the President of Ecofin is present at meetings of the Eurosystem's Governing Council. The Economic and Finance Committee, an advisory body consisting of representatives from national finance ministries, national central banks and the ECB, supports this political communication at the technical level. Concern over wage developments in the euro-zone is addressed through the macroeconomic dialogue, involving the social partners. This ensures that national governments, the Eurosystem and, to a lesser extent, social partners meet regularly to exchange information and opinions.

The main instrument for the soft co-ordination of economic policies is the broad economic policy guidelines,¹² drawn up annually by the Commission and Council and adopted by the European Council. The consistency of national economic policies with the economic objectives of the Union and (in the case of participating Member States) with that of euro-zone monetary policy are then assessed. In the event of a deviation from the Guidelines the Council can – as in the recent case of Ireland – adopt a non-binding recommendation against the Member State in question. Unlike the excessive deficit procedure, the guidelines are not supported by any sanction, relying on the commitment of states and peer pressure.

The Union's approach to adjustment is manifest in the Luxembourg, Cardiff and Cologne processes. These processes are a response to – amongst other factors – the greater need for factor market flexibility under EMU (Hodson and Maher 2000a). The Union's chosen response employs an unambiguously soft policy approach (Wessels and Linsenmann, 2001), rather than seeking a transfer of competence to the EU.

¹² Art. 99(2) EC.

While each Member State faces an adjustment challenge that implies a need for greater factor market flexibility, the precise nature of such flexibility is likely to differ from one national factor market to another. Thus, while the Union encourages the pursuit of such flexibility, initiatives at the national level remain of primary importance.

Having completed this brief tour d'horizon, we can now view the open method in a broader context. It is apparent that phrases in the open method, such as peer review, surveillance, benchmarking and best practice, derive their meaning from a specific understanding of EMU. According to this viewpoint, supranational monetary policy is best complemented by an intensive transgovernmental approach to economic policy (Wallace, 2000, p. 33). This approach has three components. First, hard co-ordination mechanisms are set in place to prevent the occurrence of regional spillover. Second, channels of soft co-ordination are established between policy actors, in an attempt to achieve a consistent policy mix. Finally, a soft co-ordinated approach to adjustment is developed to increase the efficiency of policy instruments at the national level. The method was designed to implement the third component. Its first and second stages help to identify common challenges for Member States and encourage a common approach to the formation of objectives and performance indicators. If the supranational level is more significant in the first two stages, the initiative in the third stage comes from the national level. This allows Member States to tailor their policies to the precise characteristics of their economy, thus avoiding any negative side effects associated with a one-size-fits-all approach to adjustment. The final stage offers them a useful means to evaluate their progress, without recourse to legally binding measures or sanctions. In short, the open method recognizes the optimality of the national approach. By concentrating on the enablement of individual Member States, the chances of achieving the Union's goals are, it is argued, maximized.

The Irish Budget

Jacquet and Pisani-Ferry note that the undeniable efforts taken so far have not succeeded in creating a genuine culture of co-ordination in relation to economic policy (Jacquet and Pisani-Ferry, 2001, p. 12). This can be seen in one of the first tests of the economic policy architecture when Ireland became embroiled in a controversy over the compatibility of its economic policy with the broad economic policy guidelines. In June 2000, the Council recommended that the Irish government adopt an anti-cyclical stance against overheating conditions in the economy. The next Irish budget, the last before a general election, included a series of tax cuts and allowance increases that amounted to an annualized cost of 1.5 per cent of GDP. This was matched on the expenditure side with an 18 per cent increase in voted current expenditure and a 29 per cent increase in voted capital expenditure. The update of the Irish stability programme, released on budget day, projected a reduction in the general government surplus as a percentage of GDP from a surplus of 4.7 per cent in 2000 to a surplus of 4.3 per cent in 2001. Ecofin issued a formal recommendation that identified two main sources of inconsistency between the guidelines and the budget. First, the direct tax cuts were unlikely to induce greater labour force participation in an already tight labour market. Given the current monetary stance in the euro-zone, such fiscal policy was inappropriate to the overall macroeconomic policy mix. Second, the expenditure side of the budget generated a pro-cyclical rather than an anti-cyclical fiscal stance. Thus Ecofin suggested that the government take

‘countervailing budgetary measures during the current fiscal year ... to ensure that no reduction in the underlying budgetary surplus from 2000 takes place’ (Ecofin, 2001).

The Irish government’s initial response criticized the recommendation on grounds ranging from economic logic to the covetousness towards Ireland’s booming economy. Although the doubts about the ratification of the Nice Treaty following Ireland’s censure might have been thought to be scare-mongering by Irish officials, the negative result in the referendum, two days after the Council was to meet to consider the Irish position, pointedly demonstrated the importance of issue-linkage in the European context. So far, Ireland has not taken any corrective budgetary action, with the Finance Minister stating that ‘the concerns expressed in the Recommendation were based on the wrong premise’ (McCreevy, 2001). His case is strengthened by the OECD’s recent suggestion that Irish estimates of its government revenue for 2001 were excessively cautious (OECD, 2001). It suggests that Ireland’s budget for this period will be ‘roughly neutral’, thus contradicting the broad economic policy guidelines (and indeed the Irish stability programme). These differences show the capacity for divergent opinion in relation to the guidelines and the difficulty, if not impossibility, of clearly identifying policy as right or wrong.

The soft policy foundations proved no obstacle to communication, as the Irish case occupied considerable media attention. The Wall Street Journal, defending Ireland’s position, had an article by the Irish Finance Minister and a comment by the leading supply-side writer, Arthur Laffer (Gillespie 2001). Policy communication was not a problem for Ecofin, although it was for the Commission, which was to some extent scape-goated by the Council in the light of widespread criticism of the recommendation (Dyson, 2002a). What the episode shows is that co-ordination allows debate to flourish, and for a country to defend openly its own view (Mayes and Viren, 2001). While this may improve transparency, engage a wider public in the debate and shed some light on the policy processes involved, it also raises implications for democracy, with the elected government’s preferences being subject to question as a result of guidelines agreed at a supranational level. At the same time, because of the existence of EMU, national policy failure in the light of the sound finance and sound money paradigm could have serious implications for the other members of the euro-zone which do not have any direct voice at the national level and rely on the open method to avoid having any consequent burden shifted on to them. While such a risk of burden-shifting is real in the case of larger states, it is insignificant in the case of a small economy like Ireland, and the credibility of the system is thus undermined by the application of the same rules to large and small economies, irrespective of their relative effects on the euro-zone. Although Ireland will escape any form of binding sanction, the true costs of its actions have yet to be established, the situation being so recent as to be necessarily inconclusive. If Ireland suffers a lack of political goodwill from its peers and a loss of credibility in the EU as a result of its recalcitrance, then the credibility of the Union’s soft policy approach may itself increase as a consequence.

IV. The Open Method of Co-ordination as Novel

The Conditions for the Open Method

The classification of the open method as a new form of governance is not without difficulty. Lebessis and Paterson in their analysis of EU governance put forward a paradigm of collective learning that looks very like the system of open co-ordination

that we see in relation to economic policy (Lebessis and Paterson, 2001, p. 288). They suggest that collective learning goes to the heart of a new understanding of control and responsibility in EU governance. Member States face generic problems in specific contexts. The specificity of the context obscures structural components of problems, which results in a failure to understand the underlying causes of a particular problem, which are common. Calame proposes that problems be approached at a local level by describing essential features of the given context without being exhaustive (Calame, 2001). The next stage involves a comparison of the information produced in different contexts in order to identify those characteristics that are structural and those that are determined by particular context. Having identified the common structural components, the Member States then have a range of responses as to how to proceed. The policy process remains open and there is no prescribed solution. What happens within this iterative process is that common principles can be developed with a move away from control of outcome to an obligation to respect common, articulated, principles.

The experience of the open method suggests that this approach is central to a particular construction of EMU and even within EMU may be less effective for structural policy than for employment policy. This in part is because of the much broader scope of structural policy, but also on the basis that, while interdependent economies and the associated risk of economic spillover require a common solution, structural reform is not, as of yet, about interdependencies but rather about states facing similar challenges. A common solution is neither on the table nor necessarily desirable. Whether the open method can be applied effectively in other policy sectors depends on whether there are equivalent initial conditions to those which exist for economic policy. In other words, there must be a cultural frame (Fligstein and Mara-Drita, 1996), as entrenched within the Treaty as for EMU; this implies that it is best applied within the context of single market initiatives. It is this cultural frame which provided the agreed, if not entirely fixed, paradigm of sound money and sound finance (Dyson, 2000b). This made co-ordination essential for economic policy and subordinated employment policy to the sound money, sound finance paradigm such that co-ordination is now partial and focused on those aspects of employment policy which coincide most closely with this paradigm, thus with, e.g., wage policy excluded (Goetschy, 1999). The strong links between monetary policy and economic policies, where monetary policy is uniform and highly centralized, in effect mandated co-ordination of economic policy, while the diversity of national approaches required that co-ordination remain at the national level so that there is adequate room for manoeuvre in response to asymmetric shocks. Co-ordination also enjoys a long history of project-building by key elites (Dyson and Featherstone, 1999), who over time develop a common discourse such that the open method is, in some sense, just another stage in previous iterative processes that began with the establishment of the Economic Policy Committee in 1974¹³ and the Werner Report in 1970. Co-ordination can arise only where there is support from the European Council which, in relation to economic policy, is taking a more active role following Lisbon with an additional meeting in spring each year to assess co-ordination. The central role of the European Council also underlines the intergovernmental nature of co-ordination and ensures that processes remain open in terms of outcomes, such that there is no attempt to centralize policy formation or to introduce top-down methods of integration.

¹³ Council Decision 74/122/EEC, OJ L 63, 5.3.1974, p. 2 setting up the EPC.

A Transitional Mechanism?

A permanent system of innovation in policy formation – through refinement of existing practices or introduction of new ones like the open method – is not transitory unless there is a transfer of competence to the EU. The open method may lead to the formal reassignment of policy powers from the national to the EU level and hence may not provide a durable alternative to the traditional EU model. At this stage it operates as a form of negative co-ordination, with monitoring and peer pressure ensuring compliance of national policy instruments through agreed commitments, rather than as a form of positive integration with agreement on a specific policy approach at the EU level (Dyson, 2002a, Scharpf, 1999, ch. 2). The emphasis is on not engaging in certain policies rather than agreeing a specific supranational policy and then implementing it at the national level. The methodology of learning by benchmarking and best practice means Member States must redefine their economic policy by taking the lead in opinion formation with a view to acting as a catalyst in the formation of ideas (Dyson, 2000a, p. 5). The system, in short, seeks to make a virtue out of the inevitable and continuing diversity institutionally and ideationally in the way that Member States define and conduct their economic policy. This means that any importing of policy ideas as a result of co-ordination is conditional on the question of ‘fit’, i.e. the extent to which the existing policy framework is consistent with any proposed change (Dyson, 2000a; Maher, 1996), or on the extent to which an effective transition mechanism is built into the new policy frame. The emphasis on iterative processes removes the traditional intergovernmental emphasis on great moments, pointing instead to a policy learning continuum, thus introducing the prospect of incremental change and making it a less risky prospect. The extent to which the open method is a new, durable form of governance depends on the extent to which the process can remain open and tolerate partial, fragmented and interim outcomes, formulated in the knowledge that dialogue will continue (Shaw, 1999, p. 338). Co-ordination as a form of inter-administrative governance may lead to the exchange of ideas and the emergence of a common discourse for the ‘club’ of key officials and ministries involved (Levitt and Lord, 2000, p. 217), such that policy transfer is made easier as a result of the reframing of domestic discourse over time (Dyson, 2000b, p. 649). This process of informal institutionalization of national administrations and their common interest in finding common solutions to common problems through deliberative interaction could be described as deliberative supranationalism (Joerges and Neyer, 1997).

Within the sound money, sound finance paradigm, the rejection of transfer of competence in the field of factor market policy appears as a necessary truth. The history of economic and monetary integration shows that necessary truths can appear contingent in the presence of changing conceptual paradigms (Quine, 1951). This means that if a ‘window of opportunity’ emerges (Kingdon, 1984), it may result in a shift in belief systems such that that which is deemed impossible now, e.g. the transfer of employment policy (including wage policy) to the EU, may become possible. Co-ordination could become a form of positive integration with policy transfer to the European level. While this suggestion points to a co-ordination-begets-integration model, even in the face of the Irish experience and the conflict it generated, it is nonetheless important to remember that by its very nature the open method does not preclude a shift to positive co-ordination, no matter how unlikely that looks in the current political and economic climate. Should there be such a shift, the open method

could be seen as a transitional mechanism leading to transfer of competence and a pre-cursor to other, more familiar forms of EU governance.

V. Conclusion

The open method provides both functional and political advantages (Mosher, 2000). On a functional level, it emphasizes policy change by states, but recognizes that there may be collective action problems blocking progress or that collective responses might reduce costs. Several or all states might wish to move in tandem, or at least instigate reform in the knowledge of each other's practices and agendas. The open method thus allows both co-ordinated and individual responses, as appropriate with the possibility of convergence, but with an emphasis on policy learning. However, the Irish case study shows that individual responses are allowed only within an agreed spectrum. Politically, the open method is an alternative to traditional governance methods without precluding a return to them, and thus is not inconsistent with the revitalization of the Community method advocated by the Commission in its White Paper on Governance (Commission, 2001c, p. 29). The Commission retains a role and existing Union competence is not challenged, while the possibility of further transfer of competence remains. The flexibility of the open method, which allows for policy formation best suited to national needs, albeit within the context of best practice and transparency between states, avoids problems of ill-fitting Europeanization of national policies and attendant dissatisfaction by governments and their electorates. Diversity is also its greatest weakness in that the lack of formal sanctions or binding legal norms allows states to proceed in opposition to any agreed principles (as contained in the guidelines), thus potentially undermining the credibility of this form of governance.

It is too early to say whether the open method can deliver the strategic goal of the EU as the most competitive and dynamic knowledge-based economy in the world within ten years. The experience of the Stockholm European Council of March 2001 shows that the method is advanced and working well in relation to employment policy, with the European Council setting targets for employment rates and setting up a high-level task force on skills and mobility to examine barriers in the labour market. Co-ordination is improved for the social model with indicators on work quality to be developed by the end of 2001 and work quality being included as a general objective in the 2002 employment guidelines. A two-prong approach is taken in relation to discrimination between men and women at work reflecting both hard and soft co-ordination. Indicators are to be drawn up for pay discrimination, while for other terms and conditions existing legislation will be updated by the end of 2001 (European Council, 2001). For pensions, a similar mix of hard and soft co-ordination is advocated, with reports being presented to Council at future summits and reform of Regulation 1408/71 on social security co-ordination proposed. In other sectors, e.g. enterprise policy, there are teething problems with the open method, notably recognition of the need to improve the quality, time-lines and availability of statistics for benchmarking.

The answer to the question – is the open method of co-ordination a new form of governance? – is 'yes, perhaps and no'. Yes, in the sense that in the context of EMU the open method is founded on a rejection of notions of policy transfer and thus, within the Wallace and Wallace framework, represents a novel form of integration. What is also new is the explicit naming of such a method by the European Council, along with its association with a new strategic vision of the EU and its extension to

other policy areas. Perhaps, in that the novelty of the open method in other policy areas depends on the existence of similar conditions to those found in EMU. It is only if such conditions exist that the open method is likely to reject from the very outset the prospect of a transfer of competence to the EU level. No, in that, even if such conditions preclude a transfer of competence at present, the open method is by its very nature open, and may in time lead to a convergence of ideas or practices which could culminate ultimately in support for competence transfer to the EU.

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